In the Supreme Court of the United States

OCTOBER TERM, 1972

No. 72-1145

J.A. NEWSOME, JR., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The first opinion of the district court is reported at 301 F. Supp. 757. The opinion of the court of appeals, reversing and remanding the case, (Pet. App. 15-27), is reported at 431 F. 2d 742; the opinion denying a petition for rehearing with a suggestion of rehearing *en banc* is reported at 431 F. 2d 749. On remand the district court wrote no opinion. The opinion of the court of appeals affirming *per curiam* the judgment of the district court (Pet. App. 35), is reported at 468 F. 2d 1399.

JURISDICTION

The judgment of the court of appeals was entered on November 22, 1972 (Pet. App. 36-37). The petition for a writ of certiorari was filed on February 20, 1973. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the court of appeals applied correct legal principles in determining that petitioner, concededly a "responsible" officer, was liable for the penalty provided by Sections 6671 and 6672 of the Internal Revenue Code of 1954 for failure to pay over withheld taxes.

STATUTES INVOLVED

The pertinent provisions of Sections 3102, 3402, 6671, 6672 and 7501 of the Internal Revenue Code of 1954 (26 U.S.C. (1958 ed.)) are set forth in the Appendix, *infra*, pp. 9-10.

STATEMENT

Petitioner, as president of New Wolf Construction Company, is conceded to have been a responsible officer of that corporation within the meaning of Sections 6671 and 6672 of the Code. Upon default by New Wolf in payment to the government of withheld taxes, the shortages were assessed against petitioner under the provisions of Section 6672. Petitioner paid a portion of the assessed taxes and filed a suit for refund, after which the government counterclaimed for the balance due. (Pet. App. 15-16.) At the first trial the undisputed evidence showed that, when petitioner examined New Wolf's November financial statements on December 27, 1961, the withheld taxes owed to the government were approximately $20,700 and the cash then available for satisfaction of this liability was $7,739.59. (Pet. App. 25-26.) During January, 1962, more than $64,000 was deposited to New Wolf's account (Pet. App. 26, fn. 14); despite his knowledge of the liability for the withholding payments, however, petitioner permitted New Wolf to pay its creditors other than the government (Pet. App. 26).

On January 29, 1962, petitioner was informed that New Wolf did not have sufficient funds to pay the withholding

liability due for the quarter ending December 31, 1961, and, on advice of counsel, he sent to the Internal Revenue Service the required return form with an explanatory letter that full payment of the amount due would be made shortly. Thereafter, and until February 14, 1962 (at which time he ceased to have control over New Wolf's financial operations (Pet. App. 16)), petitioner continued to allow New Wolf to make substantial payments to creditors (including himself) other than the government. (Pet. App. 24, 27.)

Notwithstanding these facts, the district court held that taxpayer's reliance upon the advice of counsel was sufficient "reasonable cause" to negate a willful failure to pay over the withheld taxes within the meaning of Section 6672 of the Code. The court of appeals reversed, pointing out that petitioner's counsel had never advised him that he could legally pay out New Wolf's funds to non-government creditors without subjecting himself to liability under Section 6672 (Pet. App. 24-25, 27), and remanded the case for a determination of the amount of the judgment. (Pet. App. 27, fn. 16.) Petitioner's petition for a rehearing was denied. (Pet. App. 28-32.) After a hearing in the district court, judgment was entered in favor of the United States in the amount of $18,735.71. (Pet. App. 33-34.) Both petitioner and the government appealed to the court of appeals. The court of appeals affirmed, without opinion, the judgment of the district court. (Pet. App. 35.)[1]

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[1]The government has not sought a writ of certiorari with respect to that portion of the court of appeals decision adverse to it.

ARGUMENT

The decision below, holding that petitioner willfully failed to pay over the withheld taxes in question, is correct. There is no conflict or other reason for further review.

1. Under Sections 3102 and 3402 of the Internal Revenue Code of 1954, Appendix, *infra*, an employer is required to withhold federal income and social security taxes from the wages of his employees. These withheld funds, which are held by the employer as a collection agent for the government, constitute a special trust fund in favor of the government, Sec. 7501 of the Code, Appendix, *infra*, p. 10, and are not ordinarily considered funds available for distribution to the company's creditors.[2] Where the employer has withheld income and social security taxes, the employee is credited with payment of the appropriate amounts to the government and, unless the government has recourse against the responsible officer, when the amounts are not paid over to the government by the corporation, the tax is lost. *Dillard* v. *Patterson*, 326 F. 2d 302 (C.A. 5); *United States Fidelity & Guaranty Co.* v. *United States*, 201 F. 2d 118, 120 (C.A. 10). In order to insure that the government does not suffer such a loss, Section 6672 of the Internal Revenue Code, Appendix, *infra*, provides, that any person required to withhold and pay over these taxes (*i.e.*, a "responsible officer") who willfully fails to do so is liable for a penalty equal to the amount of the delinquency.

2. Petitioner argues that the decision below is in conflict with the rule in other circuits; in support of this con-

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[2]This may not be true after an employer who has failed to segregate the withheld taxes goes into bankruptcy, *United States* v. *Randall*, 401 U.S. 513. See *infra*, pp. 6-7.

tention, petitioner cites, for example, language from *Bloom* v. *United States*, 272 F. 2d 215, 223 (C.A. 9), certiorari denied, 363 U.S. 803, to the effect that willfullness under Section 6672 entails a "voluntary, conscious, and intentional act." (Pet. 7.) While petitioner is correct in stating that this is the rule followed and adopted in other circuits, it is also the rule followed by the Fifth Circuit in the instant case.[3] Petitioner's assertion of a conflict seems to rest upon a construction of the language quoted from *Bloom* as meaning (Pet. 13) that the responsible officer must intend that the payments which he makes to other creditors will cause the government to be deprived of its taxes. This is not, however, what was meant by the Ninth Circuit in *Bloom*, or by the other circuits following that precedent. Rather, the requisite willful preference is made when the officer pays other creditors at a time when he knows the United States has a present claim for the funds held by the employer subject to the Section 7501 trust. It is not relevant whether the officer has an intention to deprive the United States of its taxes (see *Monday* v. *United States*, 421 F. 2d 1210, 1214-1215 (C.A. 7)), or whether he hopes or expects that ultimately funds will become available to pay the government. Indeed, the facts here are in the same pattern as in *Bloom* and the other cases cited by petitioner, and we suggest that the same result would have been reached by those courts had the instant case been before them. The only payments for which petitioner has been held liable are those made by him after December 27, 1961, the date on which he was apprised that there were insufficient funds on hand to pay the withholding taxes for the fourth quar-

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[3]Significantly, the language quoted from *Bloom* is the same language used by the Fifth Circuit in its first opinion in the instant case. 431 F. 2d. at 745.

ter of 1961.[4] With respect to the payments made to creditors after that date, petitioner's counsel did not, as the court of appeals noted, *supra,* p. 3, advise petitioner that these payments could be made without the risk of liability under Section 6672.

3. Petitioner also contends (Pet. 9-10) that the decision below is in conflict with *United States* v. *Randall,* 401 U.S. 513. In *Randall,* this Court held that, in a bankruptcy situation, Section 64(a)(1) of the Bankruptcy Act (11 U.S.C. 104(a)(1)), which provides a special priority for expenses incurred in administering a bankrupt's estate, preempts even the special right of the government to funds held in trust by the bankrupt pursuant to Section 7501(a) of the Code. That holding, which emphasized repeatedly the importance of honoring in bankruptcy proceedings the priorities explicitly set forth in the bankruptcy laws, does

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[4]While we believe that there may be an inconsistency in approach between the Fifth Circuit's decision in the instant case and that of the Ninth Circuit in *Dudley* v. *United States,* 428 F. 2d 1196 (see the government's petition for rehearing in *Dudley*) (Pet. App. 40-45), the decision in the latter case seems to have been controlled by the very special circumstance that the responsible officer there had issued a check to the Internal Revenue Service covering the taxes due and the check was dishonored by the bank for reasons which the appellate court noted were not clear. The court was impressed by this and by the fact that the government was dilatory in presenting the check for payment and failed to notify the responsible officer that it had been dishonored. As the court pointed out, other funds were available after the date of issuance of the check from which the officer could have satisfied the government's claim if he had been timely notified of the dishonor. In view of the fact that, in other cases (notably *Bloom, supra*), the Ninth Circuit has taken a position which is in line with that of the Fifth Circuit here, and since the special facts in *Dudley,* with respect to which the government did not seek certiorari, tended to prevent a square presentation of the point at issue here, there is no reason to believe the Ninth Circuit would not have reached the same result as did the Fifth Circuit on the facts of the instant case.

not undermine the principles upon which the court below and other courts of appeals have relied in interpreting Section 6672 of the Code outside the context of bankruptcy.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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APRIL, 1973.

APPENDIX

Internal Revenue Code of 1954 (26 U.S.C. (1958 ed.)):

SEC. 3102. DEDUCTION OF TAX FROM WAGES.

(a) *Requirement.*—The tax imposed by section 3101 shall be collected by the employer of the taxpayer, by deducting the amount of the tax from the wages as and when paid. * * *

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SEC. 3402. INCOME TAX COLLECTED AT SOURCE.

(a) *Requirement of withholding.*—Every employer making payment of wages shall deduct and withhold upon such wages * * * a tax equal to 18 percent of the amount by which the wages exceed the number of withholding exemptions claimed, multiplied by the amount of one such exemption as shown in subsection (b)(1).

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SEC. 6671. RULES FOR APPLICATION OF ASSESSABLE PENALTIES.

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(b) *Person Defined.*—The term "person", as used in this subchapter, includes an officer or employee of a corporation, or a member or employee of a partnership, who as such officer, employee, or member is under a duty to perform the act in respect of which the violation occurs.

SEC. 6672. FAILURE TO COLLECT AND PAY OVER TAX, OR ATTEMPT TO EVADE OR DEFEAT TAX.

Any person required to collect, truthfully account for, and pay over any tax imposed by this title who

willfully fails to collect such tax, or truthfully account for and pay over such tax, or willfully attempts in any manner to evade or defeat any such tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over. No penalty shall be imposed under section 6653 for any offense to which this section is applicable.

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SEC. 7501. LIABILITY FOR TAXES WITHHELD OR COLLECTED.

(a) *General Rule.*—Whenever any person is required to collect or withhold any internal revenue tax from any other person and to pay over such tax to the United States, the amount of tax so collected or withheld shall be held to be a special fund in trust for the United States. The amount of such fund shall be assessed, collected, and paid in the same manner and subject to the same provisions and limitations (including penalties) as are applicable with respect to the taxes from which such fund arose.

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